



# SOLVENCY II USE TEST WORKSHOPS

19 & 20 March

# AGENDA

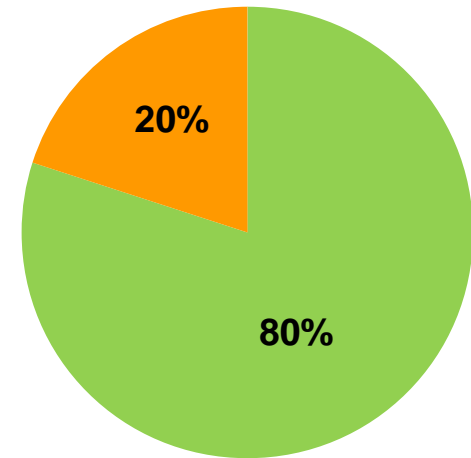
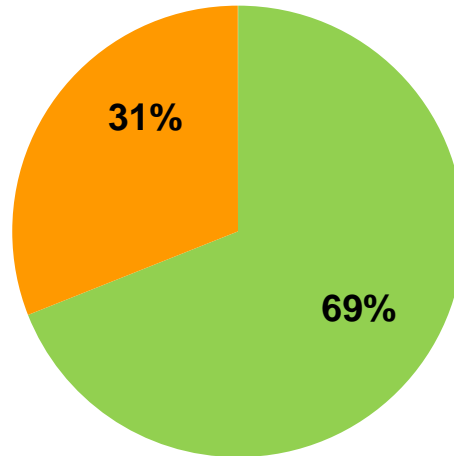
- ▶ **Introduction & Update on FAS process**
- ▶ Use Test
  - Work undertaken
  - Key themes
  - 2013 Expectations & Implications
- ▶ Table Discussion
- ▶ Update on Risk Assurance
- ▶ Next Steps

# FAS ASSESSMENTS COMPLETE AND POSITION AS AT 31 JANUARY CONFIRMED TO FSA AND AGENTS

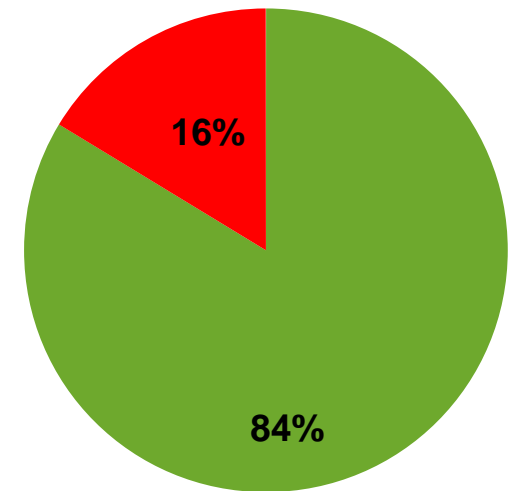
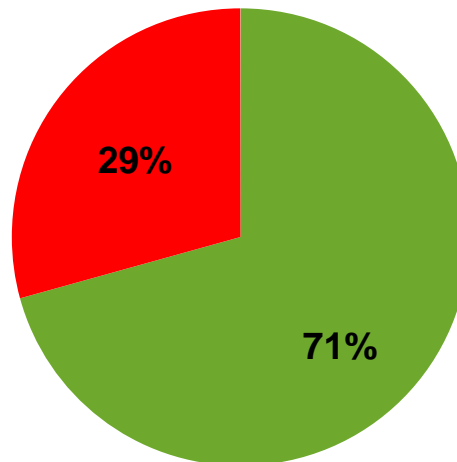
## By Agent



## By 2013 SCR

**RAG RATINGS @  
31 JANUARY**

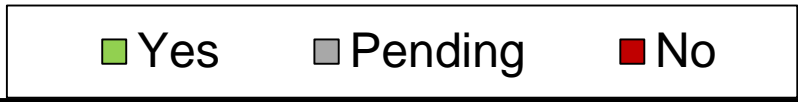
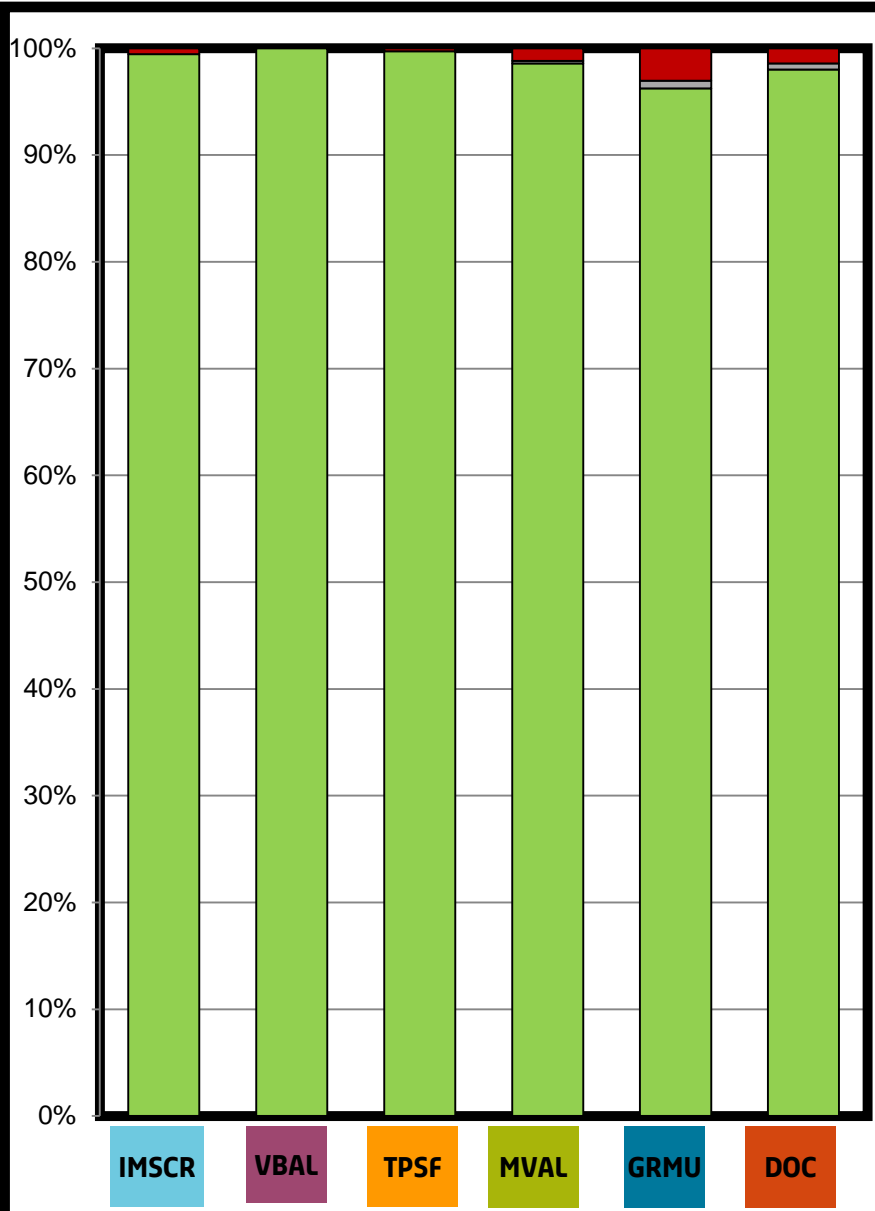


**DROP ASSESSMENTS  
TO 31 JANUARY**

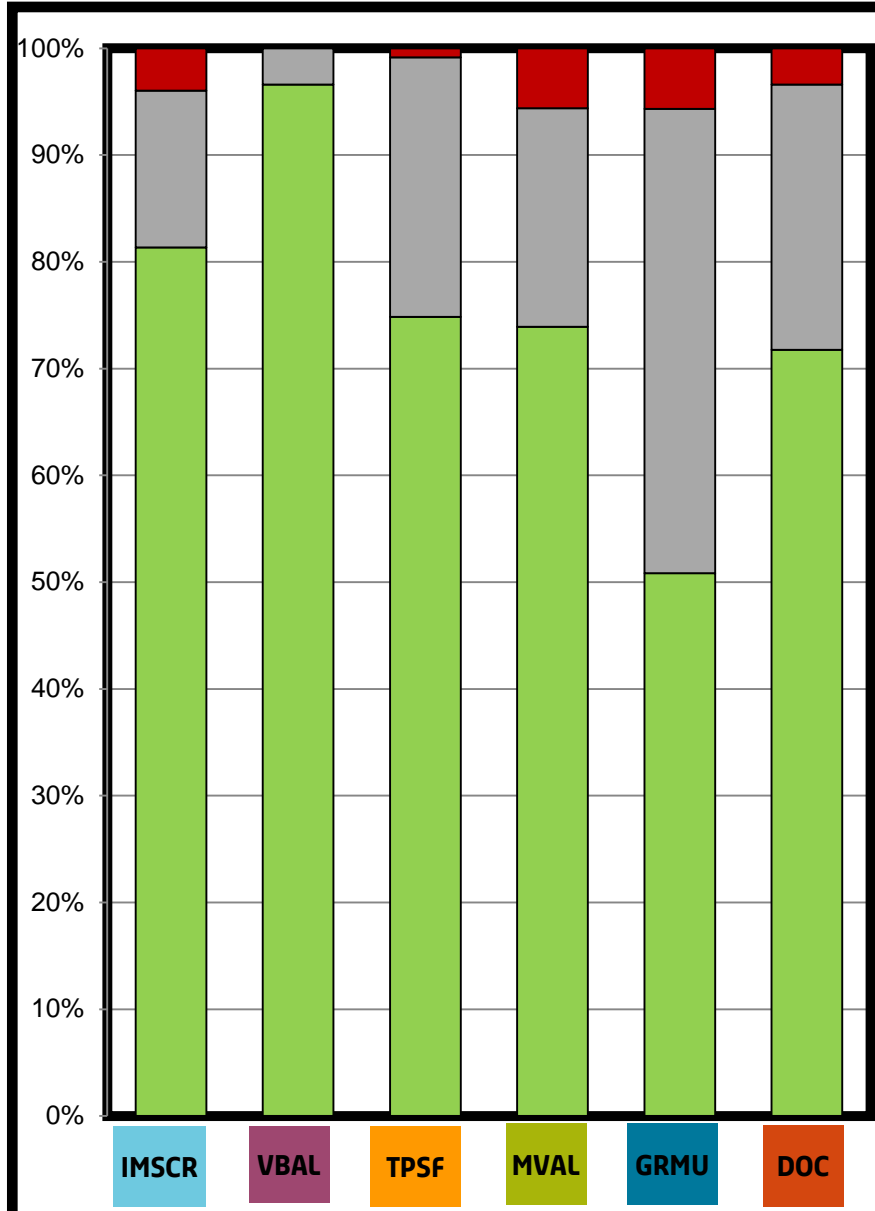


	Meets principles
	Does not meet principles

# STATUS ON "PRINCIPLES"



# STATUS ON FULL TESTS & STANDARDS



# COMMON ISSUES DRIVING “FAILS” ON PRINCIPLES

AREA/PRINCIPLE	ISSUES OUTSTANDING
<b>Validation</b>	<ul style="list-style-type: none"><li>• Lack of evidence of feedback loop and follow up/tracking of validation failures</li><li>• Validation report does not provide sufficient evidence of validation work performed and conclusions</li></ul>
<b>Use Test</b>	<ul style="list-style-type: none"><li>• Interviews did not support understanding of model or effectiveness of board training</li><li>• Lack of evidence of actual model use outside of running SCR</li></ul>
<b>Model Change</b>	<ul style="list-style-type: none"><li>• Outstanding feedback not fully addressed</li></ul>
<b>ORSA</b>	<ul style="list-style-type: none"><li>• Outstanding feedback not fully addressed</li></ul>
<b>Documentation</b>	<ul style="list-style-type: none"><li>• Submitted documents do not support controls and processes established</li><li>• Documents do not explicitly cover tests and standards requirements</li></ul>

# FEEDBACK LOGS WILL CAPTURE AND TRACK ALL OUTSTANDING REVIEW FEEDBACK

- ▶ Issued to agents initially as a basis for discussion and agreement
  - agent/Lloyd's to agree and keep up to date throughout 2013
- ▶ Lloyd's record of all outstanding feedback from reviews undertaken to date
  - new issues will be added as review work progresses in 2013
- ▶ Make clear what feedback impacts the tests & standards versus developmental
  - agree what will be actioned and when so issues can be closed
- ▶ Any “principles” issues need to be addressed asap
  - targeting end Q1 but recognise some work (eg on use test) may take longer
  - likely to require resubmission of relevant documentation to close
- ▶ Other feedback should be reflected in next timetabled submission unless interim submission date agreed

# FURTHER REVIEW WORK SCHEDULED IN 2013 AGAINST FULL TESTS & STANDARDS

AREA	TIMETABLED REVIEW WORK
ORSA	<ul style="list-style-type: none"><li>• updated ORSA reports due 28 March</li><li>• link to business plan and strategy</li><li>• follow up with agents</li></ul>
Actuarial Function	<ul style="list-style-type: none"><li>• AF Reports due 19 April in support of year end technical provisions</li></ul>
Model Change	<ul style="list-style-type: none"><li>• testing practical application</li><li>• change reports due 12 July</li></ul>
Validation	<ul style="list-style-type: none"><li>• final validation report due 26 September (in support of final SCR)</li><li>• voluntary interim submission 4 July</li></ul>
Use	<ul style="list-style-type: none"><li>• further follow up with all agents in H2 2013</li></ul>

# SOFT LANDING DOES NOT REQUIRE FULL COMPLIANCE WITH ALL TESTS AND STANDARDS IN 2013 BUT...

- ▶ ...Agents should continue to run and embed processes in 2013 as per operating model
- ▶ Key processes expected to be live and evidenced in line with agreed policies e.g.:
  - Model Change governance and reporting
  - Documentation controls and updates
- ▶ Important to maintain compliance with principles
  - continue to close gaps against tests and standards
- ▶ Operating model documents should continue to be refined
  - reflect Lloyd's feedback
  - update as processes are refined



# AGENDA

- ▶ Introduction & Update on FAS process
- ▶ **Use Test**
  - Work undertaken
  - Key themes
  - **2013 Expectations & Implications**
- ▶ Table Discussion
- ▶ Update on Risk Assurance
- ▶ Next Steps

# OVERVIEW OF WORK UNDERTAKEN

- ▶ 3 key strands of review activity
  - Agent self-assessment of its approach to Use Test
  - Review of relevant Use Test documentation
  - Interviews with agency directors and staff
  
- ▶ Interviews conducted broadly fell into 3 categories
  - Non-Executive Directors
  - Executive Directors – outside of the control functions
  - ‘Users’ of the model – underwriting, claims, reinsurance, finance etc.

# INTERVIEW SELECTION AND BREAKDOWN







- ▶ Idea was to meet people outside of the Solvency II programme
- ▶ For the largest agents, generally 3 interviews (2 Board and 1 User)
- ▶ For smaller agents, 2 interviews (1 Board and 1 User)
- ▶ Intention was to gain a spread of roles across the market

FUNCTION PERFORMED	PERCENTAGE OF INTERVIEWEES
ACTUARIAL	0%
CEO	13%
CLAIMS	7%
EXPOSURE/CAT	1%
FINANCE	6%
INED	23%
INVESTMENT/TREASURY	1%
NED	4%
NED (GROUP)	1%
OPERATIONS	2%
REINSURANCE	9%
RISK/COMPLIANCE	0%
UNDERWRITING	31%

- ▶ c. 140 interviews undertaken across the market

# BASIS OF REVIEW WORK UNDERTAKEN

The review activity was considered against each element of the latest requirements:

Area	Current progress
Use of the Internal Model	
Fit to the business	
Understanding of the internal model	
Supporting decision making	
Integration with risk management	
Frequency of calculation	

# KEY OVERALL THEMES

- ✓ Process helped form our view on expectations from each 'group' interviewed
- ✓ Unsurprisingly, varying approaches to meeting the use test requirements adopted across the market
- ✓ Significant training has been undertaken
- ✓ Strong use in key areas
- ✓ Good mix of stochastic modelling and expert judgement
- ✗ Evidence focused on CCK use rather than the wider model
- ✗ Differences in levels of preparedness of some interviewees
- ✗ Timing of model development means that it is difficult to evidence a lot of model use
- ✗ We feel that more work is needed for all agents to meet the 'tests and standards'

# USE OF THE INTERNAL MODEL

## OBSERVATIONS

- ✓ Key uses identified were:
  - SCR calculation
  - Business planning
  - Reinsurance planning
- ✓ Good planning for potential future uses in 2013 e.g.
  - Remuneration review
  - More granular capital allocation
  - More detailed risk appetite metrics
- ✗ Significant variation in level of use even around these uses
- ✗ Some use opportunities missed during 2012 e.g. business planning

# FIT TO THE BUSINESS

## OBSERVATIONS

- ✓ Generally, models have been developed to align to specific business models
- ✓ Alignment between use of model for business planning and granularity of output
- ✗ Variable granularity of model inputs and outputs
- ✗ Data limitations key driver of granularity
- ✗ Limited knowledge of specific limitations of the model – very generic answers provided on model limitations

# UNDERSTANDING OF THE INTERNAL MODEL

## OBSERVATIONS

- ✓ Good level of expert judgement employed, with appropriate controls
- ✓ Appropriate forums in place to challenge and discuss model outputs
- ✓ Good interaction between the actuarial function and wider business
- ✓ Good understanding of when the models should be run to aid wider decision making
- ✗ In general, 'users' appeared better prepared for our discussions than Directors
- ✗ All agents had embarked on training but the impact and success of that appeared variable
- ✗ Limited attempt to assess knowledge and effectiveness of training programmes



# INTERNAL MODEL TO SUPPORT DECISION MAKING

## OBSERVATIONS

- ✓ Good examples of use of the model to aid ad hoc decision making:
  - New business lines
  - Augmentation of approach to risk appetite
  - Capital implication of mergers and acquisitions output driving different approaches
- ✓ Good examples of the model output driving different approaches:
  - Redesigning reinsurance programmes
  - Exiting loss making business lines
- ✗ Further clarity needed on how model output should be used to drive a decision i.e. the role of expert judgement and healthy scepticism
- ✗ Documentation capturing model use varied significantly.

# INTEGRATION WITH RISK MANAGEMENT

## OBSERVATIONS

- ✓ As expected, strong integration between risk management approaches, functions and the internal model
- ✓ Appropriate governance around the risk management framework
- ✓ Well embedded systems of risk and control assessment
- ✗ Knowledge of the relevance and importance of these assessments was often limited
- ✗ Modelling methodology for operational risk often quoted as a weakness

# FREQUENCY OF CALCULATION

## OBSERVATIONS

- ✓ All agents running the model at least annually for SCR purposes
- ✓ A number of agents also achieving monthly runs
- ✓ Number of simulations was a key driver of model run time
- ✗ Intention of many agents to run a quarterly ORSA but not all currently achieving that in practice
- ✗ Speed of model run was variable from 45 minutes to days and over a week
- ✗ Model run time was a very common area of further development

# 2013 EXPECTATIONS & IMPLICATIONS

- ▶ Further work is required in 2013 and onwards to fully meet the requirements of the Use Test.
- ▶ Key review area which will give us good indication of underlying development and level of embedding:
  - Follow up on 2012 findings
  - Review activity in Q4 2013
  - Clear links to other reviews e.g. ORSA, Model Change, Validation etc.
- ▶ Use Test cannot be considered as an isolated topic
- ▶ Use Test failings may lead to additional review activity in other areas e.g. governance, risk management etc.

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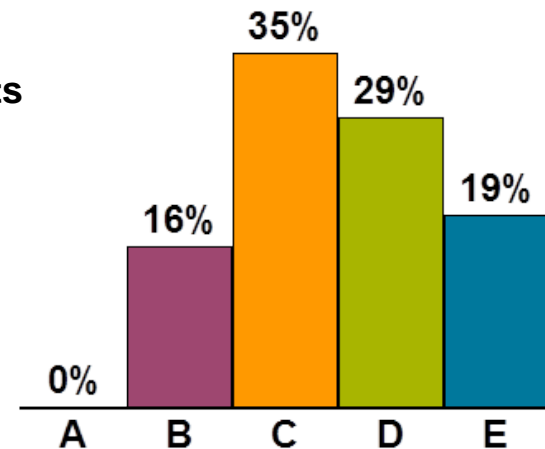
# SUGGESTED DISCUSSION TOPICS

- ▶ Do you feel your model is sufficiently developed/efficient to support all potential business decisions?
  - How is your model output developing to ensure that you have sufficient granularity of data to support business decisions?
- ▶ What work have you undertaken or plan to undertake in 2013 to develop your approach?
  - How will your approach develop given the additional time to implementation?
- ▶ What further training are you considering to develop the knowledge in the business?
  - How will you assess the effectiveness of this training?
- ▶ How will you monitor continued compliance against the principles of the use test?
- ▶ Are there any areas in which it would be useful for Lloyd's to provide additional guidance?

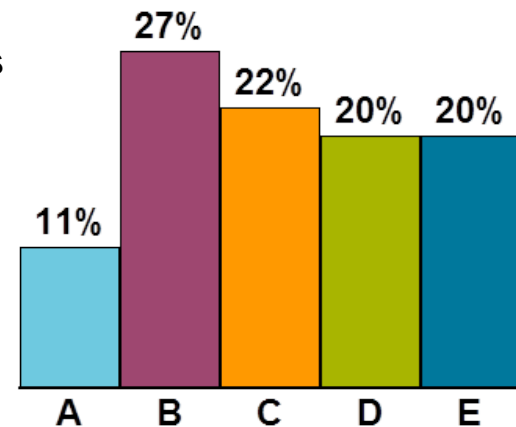
# WHICH ELEMENTS OF THE USE TEST REQUIREMENTS DO YOU CONSIDER WILL NEED MOST WORK IN 2013?

- A. SCR
- B. Business planning
- C. Validation
- D. Efficiency of model
- E. Something else

19 March Results



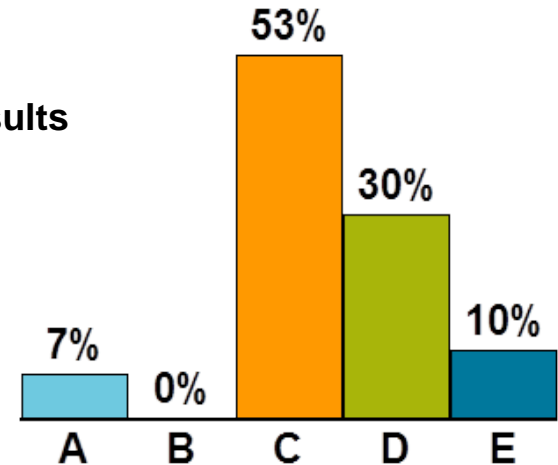
20 March Results



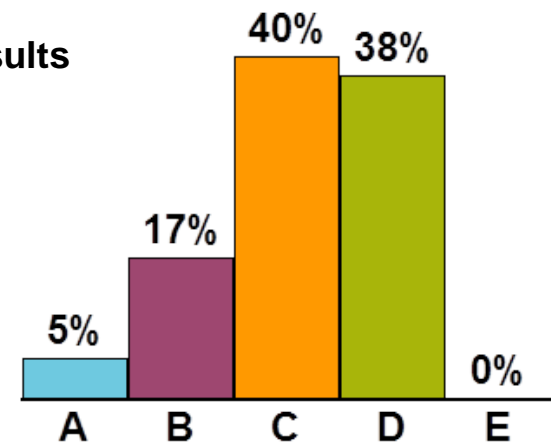
# WHAT EDUCATION DO YOU SPECIFICALLY PLAN TO UNDERTAKE IN 2013 IN RELATION TO USE TEST?

- A. Targeted Board Training
- B. Training for all relevant staff
- C. Training through BAU
- D. Other or a mix of the above
- E. No more training planned

19 March Results



20 March Results

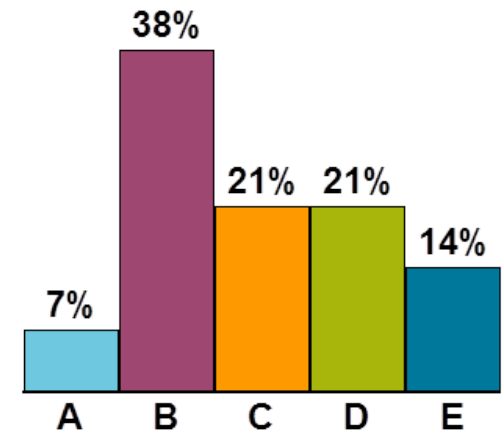




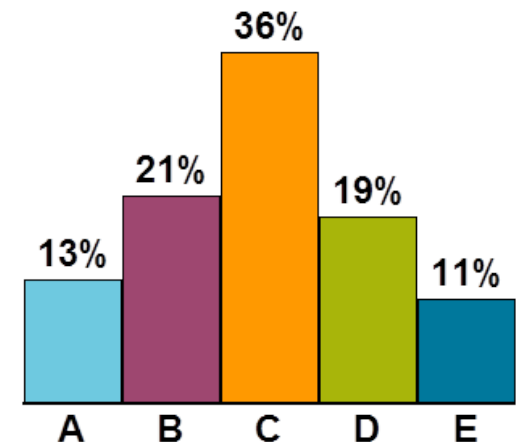
# WHICH OF THE FOLLOWING REVIEW ELEMENTS WOULD YOU LIKE TO SEE GREATER WEIGHTING GIVEN TO IN OUR 2013 REVIEWS?

- A. Board interviews
- B. User interviews
- C. Self-assessment
- D. Documentary evidence
- E. Something else

19 March Results



20 March Results



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# UPDATE ON RISK ASSURANCE WORK

- ▶ Team now established and operational within Risk Management
  - key focus in January/February has been Solvency II attestations
  - March focus is planning and assessment of standards work
- ▶ LMA Risk Assurance Committee established
  - three meetings in March to help agree scope and high level framework
  - sub groups will look at technical detail once principles of approach agreed
- ▶ Work on set up of Standards Assurance Group (SAG) in progress
  - will assume DROP role on Solvency II assessment during Q2
  - governance and direction of standards work
- ▶ Further updates will be provided as work progresses
  - Director Briefings on 17/18 April

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# WHAT HAPPENS NEXT ?

- ▶ Slides will be made available on [lloyds.com](https://www.loyds.com) after both sessions
- ▶ Upcoming submissions due:
  - 28 March: ORSA
  - 19 April: Actuarial Function Report
- ▶ Next scheduled workshop/briefings:
  - Director Briefings: 17 & 18 April (*broadened regulatory focus*)
  - Validation/Capital Setting workshop: 14 & 15 May
- ▶ EIOPA Interim Measures
  - detail for consultation expected April/May
- ▶ Market consultation sought on risk assurance as work develops
  - via LMA Risk Assurance Committee and workshop sessions

